

EXPLANATORY MEMORANDUM TO
THE FINANCE ACT 2002, SCHEDULE 26, (PARTS 2 AND 9) (AMENDMENT)
ORDER 2006

2006 No. 3269

- 1.** This explanatory memorandum has been prepared by Her Majesty's Commissioners of Revenue and Customs and is laid before the House of Commons by Command of Her Majesty.

2. Description

- 2.1 This Order provides amendments to Schedule 26 to the Finance Act 2002 (derivative contracts). The main purposes of the amendments are to
- improve and clarify the definitions of different types of derivative contracts covered by Schedule 26 FA 2002
 - add to and modify the exclusion from treatment as derivative contracts of contracts whose underlying subject matter is shares
 - modify the treatment of certain credits arising on derivative contracts as chargeable gains
 - provide a comprehensive treatment for contracts which move in or out of the derivative contracts legislation
- and generally to clarify and improve the operation of Part 9 of Schedule 26.

3. Matters of special interest to the Select Committee on Statutory Instruments

None

4. Legislative Background

- 4.1 This Order is being made as part of a continuing process of clarifying and amending Parts 2 and 9 Schedule 26 Finance Act 2002 in the light of their practical application and of issues raised by a Consultative working group.
- 4.2 This instrument relates in part to the Loan Relationships and Derivative Contracts (Disregard and Bringing into Account of Profits and Losses) (Amendment) Regulations 2006 (S.I. 2006/3236) and the Loan Relationships and Derivative Contracts (Change of Accounting Practice) (Amendment) Regulations 2006 (S.I. 2006/3238)

5. Extent

This instrument applies to all of the United Kingdom.

6. European Convention on Human Rights

The Paymaster General has made the following statement regarding Human Rights:

In my view the provisions of the Finance Act 2002, Schedule 26, Parts 2 and 9 (Amendment) Order 2006 are compatible with the Convention rights.

7. Policy background

- 7.1 Schedule 26 to the Finance Act 2002 enacted a comprehensive tax code for derivative contracts of all types. Paragraph 13 of the Schedule was originally enacted to enable the scope of Schedule 26 to be changed where new types of derivative contract were developed. In Finance Act 2005 the scope of paragraph 13 was expanded to enable it to amend Part 9 dealing with miscellaneous matters. This is because the complicated treatment of “hybrid contracts” (those which contain both debt and derivative features or are divided for accounting and tax purposes between two different elements) is included in that Part.
- 7.2 It is not appropriate to amend tax law otherwise than through legislative change, so no alternative avenues of achieving the objective have been explored.
- 7.3 There has been extensive consultation on Parts 2 and 9 Schedule 26 with relevant bodies, especially a Consultative Working Group, and this Order carries on the process of clarifying and amending those Parts in the light of their practical application.
- 7.4 Guidance on Schedule 26 generally is provided in HMRC’s Corporate Finance Manual and on its website under the heading “Accounting Standards - the UK tax implications”

8. Impact

- 8.1 A Regulatory Impact Assessment has not been prepared for this instrument.
- 8.2 There is no impact on the public sector.

9. Contact

Richard Thomas at Her Majesty’s Revenue & Customs Tel 020 7147 2558 or e-mail richard.thomas@hmrc.gsi.gov.uk can answer any queries regarding the instrument.